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No. 93-1710

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS, U.S.A.),
Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* IN SUPPORT OF PETITIONER AND BRIEF *AMICUS CURIAE* FOR NORTH CAROLINA CITIZENS FOR BUSINESS AND INDUSTRY

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MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* IN SUPPORT OF PETITIONER

North Carolina Citizens for Business and Industry hereby respectfully moves for leave to file the attached brief *amicus curiae* in this case. The consent of the attorney for the petitioner has been obtained. The consent of the attorney for the respondent was requested but refused.

North Carolina Citizens for Business and Industry ("NCCBI") was founded in 1942 as a non-profit, non-

partisan organization dedicated to the creation of a better business environment in North Carolina. NCCBI, whose members include over 1,500 companies representing every sector of the North Carolina business community, is recognized as a leading advocate of industry's position on issues affecting North Carolina business.

The decision of the North Carolina Supreme Court in this case sanctioning the use by counties of contingent fee auditors affects the rights of members of NCCBI and all other North Carolina taxpayers to fair and impartial property tax assessments.

NCCBI, through its members, has a broader perspective on the practices of contingent fee auditors in North Carolina than does the petitioner. Members of NCCBI have been audited by counties other than Cabarrus County and by contingent fee auditors other than the auditors which audited the petitioner. Also, members of NCCBI own a wider range of business property than does the petitioner, and thus the membership of NCCBI has experienced due process violations not experienced by petitioner.

Members of NCCBI have also had broader experiences with the county assessors with whom contingent fee auditors work and with the county boards which review the assessments derived from the work of contingent fee auditors.

The broad experience of NCCBI members with contingent fee auditors and the process of property tax assessment in North Carolina in general renders NCCBI uniquely capable of assisting the Court in understanding the ways in which the use of contingent

fee auditors have violated the due process rights of North Carolina taxpayers.

Respectfully submitted,

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On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

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BRIEF OF NORTH CAROLINA CITIZENS FOR BUSINESS AND INDUSTRY AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTRODUCTORY STATEMENT

This brief is submitted by North Carolina Citizens for Business and Industry as *amicus curiae* in support of petitioner in the above-captioned case. Written consent of petitioner has been obtained and has been filed with this Court. The consent of respondent was requested but refused.

INTEREST OF *AMICUS CURIAE*

North Carolina Citizens for Business and Industry ("NCCBI") was founded in 1942 as a non-profit, non-partisan organization dedicated to the creation of a better business environment in North Carolina. NCCBI, whose members include over 1,500 companies representing every sector of the North Carolina business community, is recognized as a leading advocate of industry's position on issues affecting North Carolina business.

The decision of the North Carolina Supreme Court in this case sanctioning the use by counties of contingent fee auditors affects the rights of members of NCCBI and all other North Carolina taxpayers to fair and impartial property tax assessments.

SUMMARY OF ARGUMENT

Contingent fee audit contracts used to assist in the property tax process violate the Due Process Clause of the Fourteenth Amendment because they provide an incentive to produce unfairly high tax assessments. The role of the contingent fee auditor involves the exercise of significant judgment and discretion which directly affects the final assessments issued by county assessors. The interest of the contingent fee auditor in the highest possible assessment so permeates the assessment process as to irremediably taint the assessment. This problem has been exacerbated by the fact that the work of contingent fee auditors in North Carolina has been inadequately supervised because most tax assessors have inadequate training, expertise and experience to be able to properly oversee the activities of these auditors, particularly in the complex area of personal property assessment.

The review procedure provided by North Carolina law is inadequate to remedy the due process violations inherent in contingent fee audits. Not only does the taxpayer have the burden of proof to prove that the assessment derived from the contingent fee audit was arbitrary or illegal and that the assessment substantially exceeded the true value in money of the property assessed, the taxpayer must prove this before a county board which itself has an interest in the highest possible assessment and which is highly deferential to the actions of the county assessor.

ARGUMENT

I. THE USE OF CONTINGENT FEE AUDITORS IN MAKING PROPERTY TAX ASSESSMENTS VIOLATES THE DUE PROCESS CLAUSE.

A contract that gives a person engaged in determining tax liability a direct financial interest in the amount of taxes assessed gives that person an incentive to induce the local government to issue as high an assessment as possible. The bias inherent in such a contract necessarily infects the entire assessment process and deprives taxpayers of an impartial adjudicator in violation of the Fourteenth Amendment to the United States Constitution, which prohibits the states from depriving any person of property without due process of law.

This Court held in *Tumey v. Ohio*, 273 U.S. 510 (1927), that the Due Process Clause requires that a judicial officer have no pecuniary interest in the outcome of an adjudication. *Tumey* involved a mayor acting as judge in a proceeding from which he received a percentage of the fine he imposed. This Court

stated: "That officers acting in a judicial or quasi-judicial capacity are disqualified by their interest in the controversy to be decided is, of course, the general rule." 273 U.S. at 522.

In tracing the right to a judicial officer free of pecuniary interest back to the Middle Ages, the Court stated flatly that, "the slightest pecuniary interest of any officer, judicial or quasi-judicial, in the resolving of the subject matter which he was to decide, rendered the decision voidable." 273 U.S. at 524.

The general rule is that the assessment process is a judicial or quasi-judicial process. In *Hagar v. Reclamation District No. 108*, 111 U.S. 701 (1884), this Court stated: "where a tax is levied on property not specifically, but according to its value, to be ascertained by assessors appointed for that purpose upon such evidence as they may obtain, a different principle comes in. The officers in estimating the value act judicially." 111 U.S. at 710.

The Court added that, "the duties of assessors in estimating the value of property for purposes of general taxation are judicial." 111 U.S. at 710 n.

In the instant case, the auditing work performed by the contingent fee auditor was an integral part of the assessment function. The activities of the auditor were completely interwoven with the activities of the assessor. The assessment itself was the direct result of the work of an auditor with a pecuniary interest in a high assessment. (Petitioner's Appendix 26a.)

In an *amici curiae* brief in support of the use of contingent fee auditors which was filed by the North Carolina Association of County Commissioners and North Carolina League of Municipalities with the

Supreme Court of North Carolina in this case, the *amici curiae* pointed out that approximately 27 of the 100 counties in North Carolina have used contingent fee auditors for the property tax assessment of business personal property. Thus, the use of contingent fee auditors is a pervasive practice in North Carolina.

The *amici curiae* also pointed out that with few exceptions, North Carolina counties do not employ auditors on their assessors' staffs. This lack of in-house expertise inevitably renders it difficult, if not impossible, for an assessor to effectively supervise the contingent fee auditor or evaluate the auditor's report.

It has been the experience of NCCBI members that North Carolina assessors have generally accepted, without significant change, the recommendations of contingent fee auditors, in effect merely rubber stamping their reports, which then become the assessments. Thus, the auditor, with a pecuniary interest in the highest possible assessment, is the true decision maker in most contingent fee audits in North Carolina.

Personal property tax auditing is a complex process encompassing the review of a broad range of taxpayer records and requiring the exercise of the auditor's judgment throughout the process. This exercise of discretion in large part determines the value conclusions inherent in an assessment. Contingent fee auditors auditing members of NCCBI have made decisions such as those listed below:

(a) selective decisions as to what taxpayer records to review or to exclude from review or consideration;

(b) the classification of particular items of property as real property or personal property or mixed real property and personal property. As an example, boilers for heating systems, air conditioning, wiring, venting, flooring, conveyors, shelving and displays are all items that may be considered either real estate or personalty and as such subject to different valuation techniques;

(c) the classification and valuation of items of inventory as raw inventory, work in process, or finished product;

(d) in the event that certain cost data and dates of acquisition are unavailable, the estimation of the value of particular items of personalty;

(e) the determination of whether entries on a taxpayer's books reflect property which is properly assessable;

(f) the classification of particular items of machinery and equipment into categories which have short lives and rapid depreciation resulting in lower assessments or into categories with longer lives and less rapid depreciation resulting in higher assessments;

(g) the recommendation of trending and depreciation tables used by counties to value machinery and equipment, the decision as to which may result in higher values or lower values depending upon which tables are recommended by the auditor and accepted by the assessor.

Further, in many counties, contingent fee auditors have been given broad discretion as to choice of audit

targets, invariably choosing the larger taxpayers in the county for audit.

In short, in the instant case and in other cases in which contingent fee auditors have audited members of NCCBI, the role of the contingent fee auditor has involved significant judgment and discretion, particularly given the typical assessor's lack of resources and independent expertise. An inevitable bias towards inflated assessments is inherent in this process.

II. THE COUNTY REVIEW PROCEDURE DOES NOT CURE THE DUE PROCESS VIOLATION.

The procedure required by North Carolina law and followed by North Carolina counties in reviewing a decision of an assessor is not adequate to remove the taint of the pecuniary interest of the contingent fee auditor from the assessment rendered by the assessor acting on the contingent fee auditor's recommendation.

In North Carolina, tax assessments rendered by an assessor are presumed to be correct and the burden of proof is on the taxpayer to show that the assessment is erroneous. In order to rebut the presumption of correctness, the taxpayer must produce competent, material and substantial evidence that the assessor used an arbitrary or illegal method of valuation *and* that the assessment substantially exceeded the true value in money of the property. *Appeal of McElwee, et. al*, 304 N.C. 68, 75, 283 S.E.2d 115, 120 (1981); *Appeal of AMP, Inc.*, 287 N.C. 547, 562-63, 215 S.E.2d 752, 761-62 (1975). While this burden of proof may be appropriate where the assessment is made by one with no financial interest in the outcome, it is constitutionally offensive where the assessment process

is tainted by the use of a contingent fee auditor who has a direct financial interest in the assessment. In this latter situation, the underlying basis for presuming the correctness of a tax assessment does not exist.

Under North Carolina law, an assessor's decisions are subject to review by the county commission, the elected governing body of each county, sitting as the board of equalization and review or by a special board of equalization and review appointed by the county commissioners. N.C. Gen. Stat. § 105-312 and N.C. Gen. Stat. § 105-322. If the commissioners decide to appoint a special board of equalization and review, the special board often includes members of the county commission themselves and it generally meets for only a limited period of time. At all other times, appeals from assessments are heard by the county commission.

The assessor is a county employee appointed by the board of county commissioners. N.C. Gen. Stat. § 105-294(a). The board inevitably relies on the supposed expertise of the assessor and is not likely to overturn his decision. More frequently than not, if any action is taken other than approving the assessment, in complex cases the board will merely remand the assessor's decision to the assessor for further consideration rather than attempt to resolve the case itself.

County commissioners in North Carolina are under great pressure to raise revenues in order to meet the increasing demands placed upon county governments for social services and other spending. Unfunded mandates imposed upon counties by state government also exert pressure on county commissioners to raise revenues. County commissioners are under significant political pressure to keep taxes on homeowners low. All

of these factors frequently result in the overly aggressive—and unfair—pursuit of business taxpayers.

A business taxpayer, when confronted with the necessity to appeal an inflated assessment made by an assessor based upon the recommendation of a contingent fee auditor, finds itself facing not only the burden of proof to prove that the assessment is wrong and substantially excessive, but having to meet this heavy burden before a body predisposed to approve the assessment without change in order to increase revenues in the least politically painful fashion.

The same concerns for due process that impelled the decision of this Court in *Tumey v. Ohio*, *supra*, and *Ward v. Village of Monroeville*, 409 U.S. 57 (1972), are present in this case. County commissioners, even though they do not profit personally from ad valorem tax assessments, have such a stake in the outcome of the proceedings in which a taxpayer challenges an assessment produced by a contingent fee audit that the review process cannot remove the taint of the contingent fee audit which resulted in the challenged assessment.

The experience of NCCBI members has been that the county appeals process does not remove the taint of an unfair assessment. If anything, the local appeals process exacerbates the due process violations inherent in the contingent fee audit process, given the burden of proof placed upon a taxpayer to rebut a tainted assessment not rendered by a disinterested assessor and the pressures on county commissioners to produce a balanced budget.

CONCLUSION

For all of the foregoing reasons, North Carolina Citizens for Business and Industry respectfully request that petitioner's Petition for Writ of Certiorari be granted.

Respectfully submitted,

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